

Message Text

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C O N F I D E N T I A L STATE 120386

E.O. 11652: GDS

TAGS: NATO, NAPO, OCON, AWACS

SUBJECT: NATO AWACS--BELGIAN/FRG VIEWS ON COST-SHARING

REFS: (A) USNATO 2512, 291051Z APR 77 (B) DS/ASG(77)55 \$
(C) STATE 15871, 250005Z JAN 77

1. REF A REPORTS CONTINUED BELGIAN INTEREST IN
"RESTARTING NATO AEW COST SHARING DISCUSSIONS FROM
FIRST PRINCIPLES, BASED ON RELATIVE GROSS DOMESTIC
PRODUCTS ADJUSTED FOR INDUSTRIAL BENEFITS." THIS
PROPOSAL WAS FIRST RAISED AND ELABORATED BY THE BELGIANS
IN A DOCUMENT CIRCULATED AT NATO 10 FEB (REF B). THIS
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BELGIAN INITIATIVE--FOR WHICH THEY CLAIM FRG RECEPTIVITY--
WOULD RESULT IN A REDUCTION OF THE BELGIAN SHARE IN
PROCUREMENT FUNDING FOR NATO AEW FROM THE APPROXIMATELY

2.5 PERCENT ENVISAGED IN THE LABERGE FORMULAS OF DEC 76
AND FEB 77 TO APPROXIMATELY 1.0 PERCENT, WITH A
CORRESPONDING DECREASE IN OTHER EUROPEAN SHARES AND AN
INCREASE IN THE US COST SHARE, FROM 29 PERCENT
(FEBRUARY LABERGE FORMULA) TO OVER 50 PERCENT.

2. WE RECALL THAT ON MARGIN OF JANUARY 26 QUADRIPARTITE MEETING OF FINANCIAL EXPERTS IN BRUSSELS, FRG REP ALSO

CIRCULATED A PAPER CONTENDING THAT THE US WOULD DERIVE A "DIRECT BENEFIT" OF SOME 867 MILLION US DOLLARS FROM THEN PROPOSED NATO AEW PROGRAM COSTING 2.48 BILLION US DOLLARS. THIS FRG CALCULATION WAS BASED ON THE CONTENTION THAT THE RETURNS TO THE US ECONOMY IN TAXES AND "SOCIAL BENEFITS WOULD AMOUNT TO 447 MILLION US DOLLARS FROM AWACS PRODUCTION IN US, PLUS A "SAVINGS" TO US OF 420 MILLION DOLLARS DERIVED FROM US NOT RPT NOT HAVING TO PRODUCE SEVEN US NATIONAL AWACS A/C BECAUSE OF ESTABLISHMENT OF THE NATO AWACS PROGRAM.

3. SUBSEQUENTLY, IN HIS 23 FEBRUARY LETTER TO SECDEF, FRG MOD LEBER ALSO ALLUDED TO THE ALLEGED TAX BENEFITS WHICH THE US WOULD DERIVE FROM A NATO AWACS PRODUCTION LINE, INDICATING THAT THE FRG BELIEVES SUCH "FISCAL" BENEFITS TO THE US SHOULD ALSO BE FACTORED INTO CALCULATIONS OF RELATIVE COST SHARES.

4. WE AGREE WITH US MISSION (REF A) THAT WE SHOULD UNDERTAKE NOW TO RESPOND IN AS NON-POLEMICAL FASHION AS POSSIBLE TO THESE BELGIAN AND FRG INITIATIVES. THIS MESSAGE SETS FORTH OUR VIEWS ON THE OVERALL PRINCIPLE AT ISSUE AND THEN ADDRESSES THE CONFIDENTIAL

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SPECIFICS IN THE BELGIAN AND FRG POSITIONS AS WE UNDERSTAND THEM. PLEASE PASS THE SUBSTANCE OF THIS MESSAGE TO DR. LABERGE AND TO THE BELGIAN AND FRG DELEGATIONS IN BRUSSELS. FOR EMBASSIES BRUSSELS AND BONN: WE WOULD ALSO APPRECIATE YOUR SEEKING AN OPPORTUNITY TO MAKE THESE POINTS WITH APPROPRIATE HOST GOVERNMENT OFFICIALS. COMMENTS FROM ACTION ADDRESSEES WOULD, OF COURSE BE WELCOME.

5. THE PRINCIPLE

(A) THE BELGIANS PROPOSE TO REVISE THE NATO AEW COST-SHARING FORMULA, APPLYING AS A BASIS FOR THAT FORMULA ECONOMIC CALCULATIONS WHICH THEY CLAIM TO BE MORE EQUITABLE. WE ARE NOT OPPOSED TO A SEARCH FOR A MORE EQUITABLE FORMULA THROUGH WHICH MEMBERS OF THE ALLIANCE WOULD SHARE THE FINANCIAL BURDEN OF ALL PROJECTS ACQUIRED BY THE ALLIANCE FOR THE COMMON GOOD. IN FACT, SECDEF HAS RECENTLY AUTHORIZED THAT DOD UNDERTAKE PRELIMINARY WORK ON A NEW GENERAL COST-SHARING FORMULA, WITH THE UNDERSTANDING THAT THIS EVENTUALLY PASS TO AN EFFORT WITHIN AND DIRECTED BY NATO HEADQUARTERS. HOWEVER, ASSUMING THAT THERE WOULD BE SUFFICIENT EUROPEAN SENTIMENT TO PURSUE SUCH A PROJECT, IT WOULD

CLEARLY BE A LENGTHY AND COMPLEX EFFORT. ALLIANCE

INTERESTS WOULD NOT BE SERVED BY POSTPONING A DECISION ON NATO AEW WHILE GENERAL PRINCIPLES ARE RESEARCHED, DISCUSSED AND--PERHAPS--EVENTUALLY ACCEPTED. WE THEREFORE BELIEVE DISCUSSION OF A NEW COST-SHARING PHILOSOPHY SHOULD BE DIVORCED FROM THE INSTANT PROBLEM OF NATO AWACS.

(B) E-3A AWACS FOR NATO IS THE SOLUTION TO A BROADLY RECOGNIZED AND WELL-DOCUMENTED MILITARY REQUIREMENT FOR THE ALLIANCE. AS SUCH, IT CAN NEVER BE CAST
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IN SUCH PURELY ECONOMIC TERMS AS SOLE CONSIDERATION OF BALANCE OF PAYMENTS AND FISCAL ADVANTAGE WOULD SUGGEST. IF THE ALLIANCE WISHES TO SOLVE ITS MILITARY DEFICIENCIES VS. LOW-LEVEL AIRCRAFT AT LEAST RELATIVE COST AND IN THE SHORTEST PRACTICAL TIME, AWACS IS THE ANSWER. FURTHER, THE LONGER THE AWACS AEW SOLUTION IS DELAYED, THE MORE COSTLY IT IS LIKELY TO BECOME AND THE WORSE THE ALLIANCE'S PROJECTED MILITARY POSTURE BECOMES VIS-A-VIS THAT OF THE WARSAW PACT.

(C) ALTHOUGH THE FACT THAT NATO AWACS WOULD BE LARGELY A U.S.-PRODUCED SYSTEM CAUSES ECONOMIC IMBALANCES, THESE CAN BE CORRECTED TO A CONSIDERABLE DEGREE. IT WILL BE RECALLED THAT THE COST-SHARING FORMULA ALREADY DEVELOPED FOR NATO AWACS WAS BASED ON A RECOGNITION FROM THE START THAT SOME NATIONS STOOD TO BENEFIT ECONOMICALLY MORE THAN OTHERS; ACCORDINGLY, THE PROPOSED SHARES OF THOSE BENEFITING LEAST--INCLUDING BELGIUM--WERE HALVED. WE RECOGNIZE THAT NO FORMULA COULD ELIMINATE ALL IMBALANCES. NEVERTHELESS, THOSE IMBALANCES REMAINING--WHICH IN OUR VIEW ARE NOT GREAT--ARE A LESSER PRICE TO PAY THAN POTENTIALLY IRREVERSIBLE MILITARY DISADVANTAGE. IT SHOULD ALSO BE REITERATED THAT, WHERE NATO AWACS IS CONCERNED, THE TERRITORY TO BE PROTECTED IS WESTERN EUROPE. ALTHOUGH THE U.S. IS WILLING, BOTH FOR NATIONAL AND FOR ALLIANCE REASONS, TO CONTRIBUTE A FULL FAIR SHARE TO THE NATO EUROPEAN DEFENSE, PURELY NATIONAL REASONS SHOULD URGE THE EUROPEAN NATIONS TO BE WILLING TO DO AT LEAST AS MUCH FOR THEMSELVES. WE ARE NOT ASKING EUROPEANS TO CONTRIBUTE TO NORTH AMERICAN AWACS CAPABILITY.

6. THE BELGIAN PROPOSAL

WE HAVE GIVEN SOME THOUGHT TO THE BELGIAN PROPOSAL AS OUTLINED REF B AS IT MIGHT APPLY TO THE AWACS SITUATION.
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WE DO NOT FIND THE BELGIAN PROPOSITION EITHER LOGICAL OR CONSISTENT. WHILE IT IS TRUE THAT THE SUGGESTED

CONTRIBUTION OF BELGIUM TO NATO AWACS IS ROUGHLY 30 PERCENT HIGHER THAN ITS SHARE OF TOTAL NATO GROSS DOMESTIC PRODUCT (GDP), IT IS ALSO TRUE THAT COMPARED TO OTHER MEMBERS OF THE ALLIANCE BELGIUM IS AN UNDER-CONTRIBUTOR TO THE COMMON DEFENSE. ACCORDING TO AVAILABLE DATA FROM 1976, BELGIUM'S PER CAPITA DEFENSE EXPENDITURES IN THAT YEAR WERE 207 US DOLLARS; WHILE THE NATO-EUROPE PER CAPITA CONTRIBUTION WAS 209 US DOLLARS; FOR TOTAL NATO 313 US DOLLARS; AND FOR THE US 460 US DOLLARS. BELGIUM'S DEFENSE EXPENDITURES AS A PERCENTAGE OF HER GDP IN 1976 WERE 3.1 PERCENT; FOR NATO-EUROPE, THIS FIGURE IS 3.6 PERCENT; FOR TOTAL NATO, 4.7 PERCENT; AND FOR THE US, 5.9 PERCENT. THIS WHILE BELGIUM'S GDP PER CAPITA IN 1976 WAS 6,744 US DOLLARS; NATO EUROPE 5,050 US DOLLARS; TOTAL NATO 6,529 US DOLLARS; AND THE US 7,855 US DOLLARS. ANOTHER MEASURE OF THE SITUATION IS THAT IN TOTAL NATO DEFENSE EXPENDITURES, BELGIUM'S SHARE AMOUNTS TO ONLY 1.3 PERCENT, WHEREAS HER SHARE OF TOTAL GDP IS 1.9 PERCENT. CONSIDERING ONLY NATO-EUROPE, BELGIUM HAS 4.3 PERCENT OF TOTAL GDP, BUT HER SHARE OF DEFENSE SPENDING IN ONLY 3.6 PERCENT. IT IS EVIDENT FROM THE ABOVE THAT WHILE BELGIUM COULD AFFORD TO SPEND MORE ON DEFENSE THAN THE AVERAGE OF HER OTHER ALLIES (TO THE EXTENT THAT PER CAPITA GDP MEASURES AFFORDABILITY), BELGIUM ACTUALLY SPENDS LESS. CERTAINLY WE WOULD BE PREPARED TO ARGUE THUS IN ANY DISCUSSION OF A REVISED NATO AWACS COST-SHARING FORMULA WHICH TAKES GDP AS ITS DEPARTURE POINT.

7. THE BELGIANS ALSO ARGUE THAT BELGIUM WOULD NOT BE REQUIRED TO PAY FOR AWACS 30 PERCENT IN EXCESS OF HER "ECONOMIC IMPORTANCE" AS MEASURED BY GDP BUT, IN FACT, CONFIDENTIAL

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50 PERCENT LESS, BECAUSE OF THE SMALL AMOUNT OF INDUSTRIAL COLLABORATION WHICH BELGIUM WILL DERIVE FROM THIS PROGRAM. WE DO NOT FIND PERSUASIVE THE BELGIAN ARGUMENT THAT THE PRESENCE OF THE NAPMO AND BOEING EUROPEAN AEW HEADQUARTERS IN BRUSSELS MUST BE DISCOUNTED IN ANY CALCULATION OF ECONOMIC BENEFITS. WE HAVE, ON THE OTHER HAND, AGREED WITH THE LABERGE APPROACH IN HALVING THE SHARES OF THE "NON-PRODUCING COUNTRIES," ALTHOUGH SOME MAY IN FACT, LIKE BELGIUM, DERIVE TANGIBLE ECONOMIC BENEFITS FROM NAPO AND BOEING HEAD-QUARTERS, MOBS AND FOBS, ETC. IN ANY REVIEW OF THE COST-SHARING ISSUE WE COULD JUST AS LOGICALLY ADOPT

THE VIEW THAT THESE CLEARLY IDENTIFIABLE ECONOMIC BENEFITS MUST BE TAKEN INTO ACCOUNT IN THE COST-SHARING FORMULA; AND/OR THAT THERE IS REALLY NO LOGICAL REASON WHY THE "PRODUCING NATIONS" SHOULD SHARE DISPROPORTIONATELY THE BURDEN OF A DEFENSE EFFORT TO

THE BENEFIT OF ALL.

8. EQUALLY RELEVANT TO THE BELGIAN AND FRG CONTENTIONS THAT THEY ARE BEING "OVERCHARGED" FOR NATO AWACS IN COMPARISON TO THE U.S. IS THE FACT THAT THE U.S. WILL SPEND ABOUT 1.5 BILLION DOLLARS IN R AND D FUNDS FOR AWACS, FOR WHICH THE ALLIANCE IS BEING CHARGED ONLY ABOUT 60 MILLION DOLLARS. IF WE WERE TO AGREE TO THE BELGIAN (OR FRG) COST-SHARING FORMULATIONS, WE WOULD ALSO HAVE EXCELLENT REASON TO ASK THE ALLIANCE TO CONSIDER THE TOTAL APPLICABLE U.S. R AND D EXPENDITURES ON THE PROGRAM IN CALCULATING THE U.S. SHARE. IN THE BELGIAN CASE, THE U.S. COST SHARE RECALCULATED ON THE BASIS OF GDP MIGHT RISE TO CLOSE TO 1 BILLION DOLLARS. HOWEVER, THE U.S. COULD ALSO LOGICALLY "CHARGE" THE ALLIANCE A PRO RATA SHARE FOR TOTAL R AND D, A SUM WHICH, IF CALCULATED ON THE BASIS OF A TOTAL BOEING PRODUCTION RUN OF 50-60 AIRCRAFT, COULD BE CONFIDENTIAL

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25-30 MILLION DOLLARS PER AIRCRAFT.

9. THE FRG PROPOSITION. THE GENERAL OBSERVATIONS SET FORTH IN PARA 5 AND AS WELL AS THOSE IN PARA 8 ABOVE CONCERNING R AND D RECOUPMENT APPLY EQUALLY TO THE FRG CONTENTION THAT THE U.S. DERIVES DISPROPORTIONATE ADVANTAGES FROM THE DOMESTIC PRODUCTION OF AWACS. IN ADDITION, WE HAVE ALREADY POINTED OUT (REF C) THAT IN ADDITION TO THE R AND D RECOUPMENT FACTOR, THE MAJOR PORTION OF NATO AWACS OPERATING COSTS WILL BE SPENT IN EUROPE AND THAT THESE WILL ROUGHLY EQUAL ACQUISITION COSTS OVER THE SYSTEM'S LIFE CYCLE. REGARDING THE

FRG ASSERTION THAT THE U.S. "SAVES" 420 MILLION US DOLLARS BY NOT PRODUCING SEVEN E-3A AWACS AIRCRAFT FOR THE U.S. NATIONAL PROGRAM IF NATO AWACS IS ADOPTED, THIS IMPLIES THAT SOMEHOW THE US WOULD SPEND MORE MONEY ON AWACS AND RELATED PROJECTS IF NATO DOES NOT ACQUIRE THE SYSTEM THAN IF IT DOES. THE REVERSE IS THE CASE. THE RECENT RESTRUCTURING OF THE U.S. PROGRAM TO MEET U.S. NEEDS INVOLVES A REDUCTION IN THE U.S. NATIONAL E-3A PROGRAM WHICH MAKES OBSOLETE THE ALLEGED 7 AIRCRAFT/420 MILLION DOLLARS "SAVINGS." THIS DECISION, MADE UNILATERALLY SINCE THE FRG'S SUGGESTION, MEANS THAT PRACTICALLY ALL RPT ALL FUNDS CONTRIBUTED BY THE U.S. TO A NATO AWACS PROGRAM WOULD BE IN EXCESS OF

THOSE REQUIRED FOR OUR NATIONAL E-3A PROGRAM, FOR WHICH THERE WOULD BE NO RPT NO OFFSETTING "SAVINGS."

10. CONCERNING THE OTHER PRINCIPAL FRG CONTENTION

THAT U.S. DERIVES ABOUT 25 PERCENT IN TAX BENEFITS AND 7 PERCENT IN "SOCIAL BENEFITS" FOR EVERY DOLLAR SPENT ON NATO AWACS IN THE U.S., WE HAVE YET TO HEAR AN FRG EXPLANATION HOW THESE FIGURES ARE DERIVED. IN ANY EVENT, SHOULD U.S. TAXES DERIVED
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FROM AWACS PRODUCTION IN THE U.S. BE CREDITED AS A U.S. BENEFIT, THEN CERTAINLY EUROPEAN TAXES DERIVED FROM EXPENDITURES IN EUROPE ON AWACS GROUND INTERFACE AND OPERATIONS AND MAINTENANCE OVER THE LIFE OF NATO AWACS SHOULD BE CREDITED TO THE EUROPEANS. IN ADDITION, IF SUCH CONSIDERATIONS ARE TO BE TAKEN INTO ACCOUNT REGARDING PRODUCTION OF MILITARY SYSTEMS LIKE AWACS, THEY MIGHT ALSO LOGICALLY BE CONSIDERED IN CALCULATING CUMULATIVE ECONOMIC BENEFITS IN OTHER AREAS OF COMMON DEFENSE SUCH AS STATIONING OF TROOPS. THIS POINT COULD, FOR EXAMPLE, BE MADE BY THE U.S. WITH RESPECT TO THE COST OF STATIONING U.S. TROOPS IN THE FRG, WHERE EXPENDITURES ON THE GERMAN ECONOMY ARE EXTREMELY BENEFICIAL TO THE FRG. THE EUROPEANS COULD NOT EXPECT SUCH A FUNDAMENTAL RECALCULATION OF RELATIVE ECONOMIC BENEFITS FOR PROGRAMS WHICH BENEFIT THE ALLIANCE AS A WHOLE TO BE APPLIED ON A SELECTIVE BASIS, I.E., ONLY TO PROGRAMS WHERE SUCH APPLICATIONS ARE OF BENEFIT TO THE EUROPEANS.

11. FINALLY, WE FEEL STRONGLY THAT ANY STUDY OF THE GENERAL SUBJECT OF COST-SHARING, IF UNDERTAKEN, SHOULD BE CAREFULLY PROGRAMMED WITH SUFFICIENT TIME AND RESOURCES DEVOTED TO IT TO ENSURE A DEFINITIVE CONCLUSION EMERGES. WE COULD NOT SUPPORT DELAY OF A NATO AWACS DECISION UNTIL THE OUTCOME OF SUCH A STUDY.

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